TESTIMONY REGARDING ELECTRIC INDUSTRY RESTRUCTURING
BEFORE THE U.S. HOUSE COMMITTEE ON COMMERCE

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Field Hearing
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Thank you Mr. Chairman. My name is Susan Clark and I am a Commissioner at the Florida Public Service Commission. I would like to thank the Committee for holding these "field hearings" to hear from the public on retail competition in the electric market and thank you for allowing me to speak.

I am appearing today on behalf of the Florida Public Service Commission, which is the Florida agency with jurisdiction over the rates and services of Florida's investor-owned telephone, electric, natural gas, water and wastewater utilities. I would also like to note that I am a member of the National Association of Regulatory Utility Commissioners' Committee on Electricity.

The purpose of my testimony today is to urge the Congress not to adopt legislation that mandates retail access. Rather, you should allow the current activities on retail competition occurring at the state level to progress. It is our view that states are in a far better position to decide whether, and in what way, the benefits of competition can be brought forth to all consumers of electricity.

In my comments today, I will explain what I believe are the motivating factors behind the current trend toward competition in the electric industry, and why some states are pursuing retail competition more aggressively than others. I will show you that Florida is not "just saying no" to competition, but, in fact, that Florida has embraced competition when real benefits can be derived. Further, Florida is taking steps to thoroughly explore the benefits and risks of retail competition

and addressing issues that will have to be resolved should we conclude that retail competition can, and should, be implemented. Finally, I will provide some suggestions to Congress for legislation which will facilitate state activities on retail access.

As you consider the issue of retail access, it is important to reflect on the benefits the existing structure has afforded us, why the momentum exists to restructure the industry and whether or not a new structure will bring benefits to all electric consumers.

By and large, command-and-control, rate base regulation has served the nation well. The United States as a whole has among the lowest electric rates and the highest reliability in the world. Among industrialized countries, only Canada and Sweden have lower rates and both of these countries have large hydro resources. Given the increased electrification in manufacturing, these rate and reliability differences have helped the United States' international competitiveness.

Among the various states, some have very reasonable rates and some have particularly high rates. There are a variety of reasons why different states' electrical energy costs differ. Some have low costs because of low-cost hydropower, efficient nuclear plants, close proximity to fossil fuel sources, and sound regulatory policies. Other states have high rates for reasons opposite to those just stated -- high-cost nuclear plants, long distances from fuel sources, and regulatory policies that may have increased costs beyond the true cost to serve.

Before this Committee began addressing this issue, we began to see debates break out in the high-cost states over whether traditional command-and-control regulation should be traded-in for a market-based approach. It appears that the momentum for restructuring is being driven by three things. The first is a major innovation in electric generating technology. With the passage by Congress of the 1978 Public Utilities Regulatory Policy Act, or PURPA, public utilities were

required to purchase any power produced by certified cogenerators at the utilities' full avoided costs. That is, electric utilities had to pay the cogenerators an amount equal to what it would have cost the utility to generate the same amount of electricity. This development pushed the turbine manufacturers into coupling jet engine technology with steam driven recovery boilers to produce a combined cycle power plant. These low-cost units are modular in size, can be permitted and constructed relatively easily and have become very efficient. There has been nearly a 25 percent improvement in the fuel efficiency of this technology in just the last few years.

Second, these plants came into the market at the same time natural gas prices decreased significantly. This was a match made in heaven for cogenerators and independent power producers (IPPs) who wanted to sell power to the utilities. Since the capital cost of this technology and its primary fuel cost were falling precipitously, an IPP could generate power from these combined cycle units at about 3 cents per kWh. Keep in mind that this figure does not include any transmission, distribution, overhead, or administrative costs. Thus, PURPA and the resultant technology shift have led to a situation where these IPPs are now in a position to seek large industrial users who perhaps are paying as much as 9.5 cents under a retail rate to their local utility. In economic terms, the marginal cost for new production has become less than average rates and there is now an incentive to bypass the local utility.

Finally, utilities in some states have a high cost of service, which may be due to expensive nuclear units, restricted fuel availability (that is, the fuel sources may be so far away that the cost of transporting the fuel adds to the generating cost), and regulatory policies. For example, some states, in an effort to embrace the idea espoused in the PURPA that cogeneration was to be encouraged, required their utilities to pay cogenerators amounts for electricity that have now

turned out to excessive. Some of these contracts called for payments on a KWH basis that rivaled the retail rates of other utilities. Customers of utilities subject to these high cogeneration costs had to pay those costs plus the transmission and distribution costs necessary to get the power to them. These cost disadvantages, coupled with the technology advances and the drop in natural gas prices, have provided a strong incentive for customers to by-pass their native utilities.

These conditions are not present in all states. Florida's circumstances, are, in fact, quite different from those of the high-cost states that I just described. We believe that Florida has managed its energy resources well and has acted responsibly throughout the years. For example, Florida's Power Plant Siting Act requires the Commission to determine if a power plant is needed. This statewide management of generating resources has prevented the industry from consistently having excess capacity. The process also demands that the most cost-effective alternative be followed. In recent years, generating station additions have been subject to a competitive bidding process.

With respect to cogeneration, the Commission implemented PURPA with reasonable avoided cost calculations. We held rigorous planning hearings for the purpose of identifying avoided costs and we required utilities to pay no more than that amount. The Commission also encouraged utilities to negotiate contracts with cogenerators so that utilities might be able to make arrangements for power supplies that fit better with existing supply mixes.

As for nuclear power plants, Florida has five nuclear units. We've had our share of problems with nuclear plants, but we have not experienced the problems experienced in some states. Some states found it necessary to cancel nuclear plants due to cost escalations; some states have had to prematurely shut down plants because of operational concerns. So far, our

state has not experienced anything of this magnitude. Also, Florida has been somewhat progressive in providing for nuclear decommissioning costs. Because these costs, which are significant, have been provided for over a longer period, the ongoing and future cost levels will remain at more reasonable levels.

Again, there are differences among states and it is important that this Committee take that into consideration in any future legislation. Another factor that should be taken into consideration is that states who have not embraced competition may be justified in their position. In our state, for example, it is important for this Committee to realize that Florida is no stranger to competition. We have a track record of embracing competition in the telecommunications industry and using competitive forces in the electric industry when doing so was clearly to the benefit of customers.

In the telecommunications industry, Florida immediately began authorizing competition in the long distance industry after the break-up of AT&T. In 1995, before the Congress passed its landmark Telecommunications Act of 1996, the Florida Public Service Commission went on record as urging our Legislature to allow competition in the local exchange market. We have been working very hard since then to see that customers receive the benefits originally foreseen when that legislation was passed.

In the electric industry, as early as 1978, the Commission encouraged the development of wholesale competition by establishing the Florida broker system. Basically, the broker matches utility buyers and sellers to minimize statewide generation costs. At present, 20 Florida utilities, representing virtually 100% of the generating capacity of peninsular Florida, participate in the energy broker. Since its implementation, the Florida energy broker has produced over $800

million in savings for Florida's retail customers -- savings that benefit all customers, not just large power users.

Another example of how the Florida Commission has allowed competition in the electric industry is evident in the Commission's practice beginning in the early 1990's of subjecting proposed capacity additions to competitive bidding. Florida law requires the Commission to make a finding that the state needs additional capacity before a power plant can be constructed. The Commission's practice, which has subsequently been codified in rule form, recognizes that independent power producers are very interested in participating in Florida's growing need for electricity. Our belief is that this process results in lower generating costs.

Let me be clear, Florida is not in the position of just saying "no" to competition. Florida believes that customer choice is very important. However, we believe that federal legislation mandating retail access is premature at this time. The issue is very complicated and our consideration of the issue has raised more questions than we have been able to answer. We are actively monitoring the progress of other states that are further along in the process to help answer these questions. What is clear is that a "one-size-fits-all" approach cannot adequately address each state's unique circumstances. If retail access is to be allowed, it is clear that the current levels of reliability enjoyed by Florida's customers cannot be maintained unless a plan for restructuring is carefully planned and carefully executed. I think it is significant that the states moving forward on this issue are doing so based on their particular circumstances. States should be allowed to continue to experiment with and develop their own evolutionary paths toward increased competition.

As I have indicated, Florida has not ignored the debate taking place across the nation. In

fact, we have already begun to address the issue by taking steps to mitigate stranded costs. The Florida Commission has allowed investor-owned utilities to accelerate recovery of "regulatory assets" -- costs on the utilities' books that a competitive concern might have already written-off as unproductive. The Commission has also allowed recovery of costs associated with cogeneration contracts that now have above-market prices.

The Commission and its staff have had the benefit of three electric industry forums sponsored by the University of Florida's Public Utility Research Center. These forums were for the purpose of educating the Commissioners and staff on the issues involved in electric industry restructuring. Since those forums, the Commission has established an in-house workgroup for the purpose of staying abreast of these issues and for monitoring the progress of restructuring activities in other key states. It is the Commission's hope that this workgroup will allow the Commission to identify any benefits that restructuring might bring to Florida's electric customers.

As I stated earlier, I would like to offer some suggestions for items that this Committee should consider as it ponders the question of whether to go forward with a federal policy on retail access. If federal legislation is pursued, it should focus on existing impediments to competition. For example, the fact that long-term power purchases mandated by the PURPA favor certain generation sources is inconsistent with the concept of competition as a means of achieving lowest possible cost. And if generating costs are not minimized, then the idea of customer choice becomes less meaningful. Customers should have the benefit of a market where the interaction of suppliers and consumers of electricity establishes market prices.

Also, it appears that the current restrictions imposed by the Public Utility Holding Company Act will prevent multi-state holding companies from competing effectively. The

Commission should consider reviewing these restrictions and the impact they have on effective competition.

Federal legislation should also address some important jurisdictional issues. The FERC has concluded that, under the Federal Power Act, it has ratemaking jurisdiction over retail transmission services where unbundled retail service is authorized by a state. It is our view that states should maintain jurisdiction over bundled or unbundled retail transmission. The simple act of unbundling should not cause a change in ratemaking jurisdiction in an area historically governed by the states. State commissions are in a much better position and possess the specific expertise to address ratemaking issues affecting constituent end-use customers. Our concern is that the FERC's policy will visit costs traditionally assigned to wholesale customers on retail customers.

The FERC's jurisdiction should be limited to transmission from a remote generation source to the boundary of the utility that delivers power to the end-use customer. State commissions should exert jurisdiction over the terms, conditions and prices of the transmission service that lie within the state-regulated, native utility's service territory (wheeling in) as is the current practice for bundled retail services. Where states allow retail access, the rates, terms and conditions of retail unbundled transmission service would also be regulated by the state commission. The FERC would continue to have wholesale jurisdiction over long distance transmission by interconnected utilities (wheeling out and through).

The FERC has also asserted jurisdiction over the recovery of costs stranded by state-directed, or voluntary, retail wheeling, where a state lacks authority. It is unlikely that a state with authority to direct retail wheeling will lack the authority to address the recovery of retail

stranded costs. Therefore, there is no need for FERC intervention and Congress should clarify in federal legislation that investment stranded by state directed retail wheeling is within the jurisdiction of the state. Costs for facilities that are currently under the jurisdiction of state authorities should not suddenly become the FERC's jurisdiction because retail wheeling is instituted. Again, the states are in a much better position to judge the extent and value of assets which may become stranded as a result of retail access.

Finally, the FERC has asserted primary jurisdiction over the recovery of costs stranded when a retail customer converts to a wholesale customer (as in municipalization). Congress should clarify that the primary jurisdiction over the recovery of stranded costs in these circumstances should rest with the states. These costs are being recovered in rates set by the state and the states are in a better position to determine which portion of those costs are stranded as a result of the conversion.

In summary, the Florida Public Service Commission wishes to convey to the Committee the importance of recognizing that the circumstances of individual states can be very different. These differences suggest that a one-size-fits-all approach is not the best policy for the nation's electric customers. If the Congress is convinced that this issue should be addressed in legislation, it is important that states be given the flexibility to determine if and when retail access is appropriate. Legislation should be directed at addressing existing barriers to competition found in the PURPA and the PUHCA. And finally, legislation should address issues of jurisdiction with the aim of allowing states to address their own unique circumstances.

I would like to thank you again, Mr. Chairman, for allowing me to address the Committee.

SUMMARY OF TESTIMONY BY COMMISSIONER SUSAN F. CLARK
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- The Florida Public Service Commission is the agency charged with the jurisdiction over rates and service of Florida's investor-owned telephone, electric, natural gas and water and wastewater utilities.

- As evidenced by numerous examples where Florida has employed competition to the benefit of customers, Florida is generally supportive of competition and consumer choice; however, Congress should not mandate retail access.

- Existing command-and-control regulation has served the nation well and has resulted in rates and reliability that are among the lowest in the industrialized world. If retail access is to be allowed, it is clear that the current levels of reliability and rates cannot be maintained unless a plan for restructuring is carefully planned and executed.

- Some states are already moving forward with restructuring. States should be allowed to continue to experiment with and develop their own evolutionary paths.

- There are several points that the Committee should consider if it decides to go forward with a federal restructuring policy. The Committee should focus on removing existing impediments to competition and should address important jurisdictional issues.

- The Committee should consider reviewing the Public Utility Regulatory Policy Act (PURPA) and the Public Utility Holding Company Act (PUHCA). Long-term power purchase contracts mandated by the PURPA appear to favor certain generation sources. Also, PUHCA may restrict multi-state holding companies from competing effectively.

- States should maintain jurisdiction over bundled or unbundled retail transmission.

- State commissions should exert jurisdiction over the terms, conditions and prices of the transmission service that lies within the state-regulated, native utility's service territory. Where states allow retail access, the rates, terms and conditions of retail unbundled transmission service should also be regulated by the state commission.

- It is unlikely that any state with authority to direct retail wheeling will lack authority to address stranded cost recovery; therefore, there is no need for federal intervention on the issue of stranded cost recovery.

- Congress should consider clarifying that states should have primary jurisdiction over recovery of stranded costs in situations where retail customers become wholesale customers.